IN THE

Supreme Court of the United States

October Term, 1947
No. 365

EDWARD R. DOWNING, suing on his own behalf and on behalf of all other stockholders of THE UNITED CORPORATION (of Delaware), etc.,

Petitioner,

against

GEORGE H. HOWARD, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

REPLY BRIEF FOR PETITIONER

RALPH BERNSTEIN,
551 Fifth Avenue,
New York, New York,

WILLIAM H. BENNETHUM,
Delaware Trust Building,
Wilmington, Delaware,

JOHN F. DAVIDSON,
165 Broadway,
New York, New York,
of Counsel.

JAMES R. MORFORD,
Delaware Trust Building,
Wilmington, Delaware,
Counsel for Petitioner.

INDEX

Table of Cases

IN THE

Supreme Court of the United States

October Term, 1947

No. 365

EDWARD R. DOWNING, suing on his own behalf and on behalf of all other stockholders of THE UNITED CORPORATION (of Delaware, etc.,

against

GEORGE H. HOWARD, *et al.*,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

SCOPE OF REPLY BRIEF

This brief will be confined to replying to defendants' principal contentions,* which may be summarized as follows:

---

* For convenience, the Brief In Behalf of Respondents Howard, Chubb, *et al.*, submitted by William S. Potter, Esq., will be referred to as the "Potter Brief," the Brief for Defendants Edward Hopkinson, Jr. and Others, submitted by Ralph M. Carson, Esq., will be referred to as the "Carson Brief," and the Brief for the Defendants Thorne and Others, submitted by Caleb S. Layton, Esq., will be referred to as the "Layton Brief."

1. That Petitioner's claims are based on breach of "common law" fiduciary duties and not on breach of duties created by the Public Utility Holding Company Act of 1935.

2. That the decision of the Circuit Court of Appeals below is not in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Goldstein* v. *Groesbeck, et al.*

3. That it should not be presumed that Congress intended to confer a private right of action for violation of Section 4(a).

4. That the decision of the Circuit Court of Appeals below involves merely a construction of the Amended Complaint rather than an interpretation of the Act.

5. That "lack of registration" rather than owning and exchanging securities, was the "illegal aspect" of defendants' violations of Section 4 (a).

POINT I

The defendants' contention that petitioner's claims are based on breach of "common law" fiduciary duties and not on breach of duties created by the Public Utility Holding Company Act of 1935.

This is the same point which defendants unsuccessfully urged before the Circuit Court of Appeals below as a ground for dismissing the action. There is no reason why the Amended Complaint must be based *either* on common law *or* on the Act. To the contrary, it is almost inevitable that a valid claim against the directors of a holding company based on their violations of the Act will also, under a liberal construction of the pleadings, set forth a valid claim against them at common law or in equity. Even if the conclusionary allegations to which the defendants give such exaggerated emphasis* may be deemed sufficient to cause the Amended Complaint to state valid claims at common law, the Court will look at the complaint in its entirety and grant the plaintiff whatever relief the facts set forth entitle him to. *Truth Seeker Co.* v. *Durning*, 147 F. 2d 54, 56 (C. C. A. 2, 1945); *Cohen* v. *Randall*, 137 F. 2d 441, 442-443 (C. C. A. 2, 1943); *Atwater* v. *North American Coal Corporation*, 111 F. 2d 125, 126 (C. C. A. 2, 1940); see 1 *Moore's Federal Practice*, 1946 Supp., 219. It is settled by decisions of this Court that where the same set of facts alleged in a complaint constitutes grounds for relief both at common law and under a federal statute, a federal district court has jurisdiction over the subject matter of the action. *Hurn* v. *Oursler*, 289 U. S. 238; *Armstrong Paint &*

* See Potter Brief, pp. 3-5.

Varnish Works v. *Nu-Enamel Corp.*, 305 U. S. 315. As correctly stated by the Court below (162 F. 2d 654, at p. 655):

> "It is apparent that the question which we have to settle is whether the plaintiff has stated a basis for recovery under the federal statute just mentioned. If he has, the fact that he also asserts a non-federal ground does not lose him his privilege of suing in the federal court."

The statements in the Carson Brief (at pp. 5-9) to the effect that Petitioner contends that his right of action under the Act is based upon an "enlarged * * * fiduciary obligation" of directors not to act for the benefit of interests in conflict with the interests of stockholders, is a demonstrably incorrect statement of Petitioner's position, which serves only to obscure, rather than to clarify, the issues presented by this case. The quoted language, which the Carson Brief takes out of its context, related solely to Petitioner's "Third Cause of Action", which dealt with defendants' failure to file a plan under Section 11(e) of the Act (See Brief for Petitioner, pp. 20, 41). No such argument was even suggested as to the first two causes of action, which are clearly based on breach of the express statutory prohibitions against owning and exchanging securities, contained in Section 4(a).

POINT II

The defendants' contention that the decision of the Circuit Court of Appeals below is not in conflict with the decision of the Circuit Court of Appeals for the Second Circuit in *Goldstein v. Groesbeck, et al.*

Apparently, the reason the Carson Brief sought to obscure the true basis of Petitioner's position was to lay the foundation for attempting to distinguish the case of *Goldstein* v. *Groesbeck, et al.*, 142 F. 2d 422 (C. C. A. 2, 1944), *cert. den.* 323 U. S. 739. As stated in that brief (at p. 9), the Amended Complaint in this case is based on "alleged violation of pre-existing equitable duty," whereas, as stated in the opinion in *Goldstein* v. *Groesbeck* (at p. 425), that action was "surely to enforce a duty created by the Act, since but for the Act the payment under the service and construction contracts would be innocuous enough."

But, as has been shown, the first two causes of action of the Amended Complaint are based on owning and exchanging securities in violation of Section 4(a), just as in *Goldstein* v. *Groesbeck* the complaint was based on service and construction contracts made in violation of that section. And, as in that case, the acts of owning and exchanging securities were entirely lawful prior to the passage of the Act.* It may therefore be stated in this case, as in *Gold-*

* The investigations by the Federal Trade Commission and Congressional Committees which preceded the passage of the Act had shown the social undesirability of many of the corporate relations and practices of public utility holding companies and that the then existing remedies at common law and under state statutes were inadequate to cope with them. See *Reports of Federal Trade Commission*, made pursuant to S. Res. 83, 70th Cong., 1st Sess., No. 69A, p. 357; No. 73A, pp. 1-28. But it was only upon the passage of the Act that these relations and practices became wrongful as a matter of law.

stein v. *Groesbeck,* that "but for the Act" the acts complained of "would be innocuous enough."

The Layton Brief (at pp. 14, 15) attempts to distinguish the *Groesbeck* case on the further ground that the service and construction contracts there made in violation of Section 4(a) were declared void by Section 26 of the Act, and that it therefore followed that the operating subsidiaries which paid money pursuant to such contracts had to be placed in *statu quo.* It is submitted that any such attempted distinction is without substance since Section 26 does no more than enunciate the common law rule that contracts made in violation of an express statutory provision are void (*Williston on Contracts,* Revised Edition, 1936, §1789, p. 5086) and it is therefore apparent that the Court would have reached the same result even without Section 26. Furthermore, it is to be noted that Section 26, like Section 4(a), contains no provision expressly conferring a right of action upon a private party.

The decision in *Meyer* v. *Kansas City Southern R. Co.,* 84 F. 2d 411 (C. C. A. 2, 1936), referred to at page 9 of the Carson Brief, has no application to the facts of this case since there it was clear that the anti-trust acts, and other federal statutes alleged to have been violated, gave a stockholder such as the plaintiff in that case no right to relief against the defendant directors and conferred no jurisdiction upon a federal district court to entertain such an action. See *Meyer* v. *Kansas City Southern R. Co., supra,* at p. 413. In the instant case Section 25 of the Act expressly confers jurisdiction on the District Courts over "all suits in equity and actions at law brought to enforce any duty or liability created by * * * this title." As con-

trasted with the broad jurisdictional provisions of Section 25, the provisions of the anti-trust acts relating to the bringing of actions are extremely limited and restricted. See Section 4 of the Sherman Act (15 U. S. C. A. §4) and Sections 4 and 16 of the Clayton Act (15 U. S. C. A. §§15 and 26). It should also be noted that an investor in the securities of a railroad company was not a member of a class of persons intended to be protected by those statutes, which were primarily intended for the protection of shippers, purchasers of goods in interstate commerce and the public at large. In the present case, however, Petitioner, as an investor in holding company securities, is indisputably a member of a class which the Act was designed to protect.

POINT III

The defendants' contention that it should not be presumed that Congress intended to confer a private right of action for a violation of Section 4(a).

As pointed out at pages 22 and 23 of Petitioner's Brief, it has long been settled, contrary to defendants' contention, that it *is* to be presumed that Congress intends to confer a private right of action for violation of a statutory provision even though the statute does not expressly confer a private right of action for violation of such provision.

The Carson Brief (at p. 9) argues, however, that since Congress expressly provided a private civil remedy for violations of Sections 16 and 17(b) of the Act, it should be presumed that no right of action was intended for violations of Section 4(a). This argument ignores the fact that

both the House and Senate Committee Reports clearly show that it was necessary to define with precision the extent of rights of action under these particular sections in order to avoid conflict with the corresponding sections of the Securities Exchange Act of 1934.* It also fails to take into account the express provision in Section 16(b) to the effect that "the rights and remedies provided by this title, except as provided in Section 17(b), shall be *in addition to any and all other rights and remedies* that may exist under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934 *or otherwise at law or in equity* * * *" (Italics supplied.) Furthermore, this is the type of argument described by the maxim *expressio unius est exclusio alterius* which, as this Court has recently stated, has "long been subordinated to the doctrine that courts will construe the details of an act in conformity with its dominating general purpose." See *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344 at pp. 350-351. When one considers the broad purposes of the Act to protect investors in the securities of holding companies from injuries resulting from the activities of unregulated holding companies, it becomes apparent that express reference to a civil right of action in certain limited situations was not intended to exclude the maintenance of civil actions in all other situations. Cf. *Kardon* v. *National Gypsum Company, et al.*, 69 F. Supp. 512, at p. 514 (E. D. Pa.).

---

* See Senate Report No. 621, Pub. Utility Act of 1935, 74th Cong., 1st Sess., pp. 40-41; House Report No. 318, Pub. Utility Act of 1935, 74th Cong., 1st Sess., p. 21.

POINT IV

The defendants' contention that the decision of the Circuit Court of Appeals below involves merely a construction of the Amended Complaint rather than an interpretation of the Act.

As stated in the Potter Brief (at p. 6), "the Court's decision involved merely a construction of this particular complaint rather than an interpretation in any fundamental sense of the Public Utility Holding Company Act of 1935." To the contrary, it is submitted that the question before the Court was whether a correct interpretation of the Public Utility Holding Company Act of 1935 did or did not give Petitioner a right to relief against the defendants based upon the unequivocal allegations contained in the Amended Complaint. Under the construction of the Act contended for by Petitioner, the Amended Complaint clearly set forth valid claims for relief. Under the interpretation placed upon the Act by the Circuit Court of Appeals below, it did not. The decision of the Circuit Court of Appeals, therefore, necessarily turned upon the proper interpretation of the Public Utility Holding Company Act of 1935—not upon the proper interpretation of the Amended Complaint.

If the Circuit Court of Appeals was right in holding that the Amended Complaint failed to state valid claims for relief under the Act, it was right because its restricted interpretation of the extent to which the Act was intended to impose civil liability was correct. If, on the other hand, Petitioner is right in his interpretation of the Act, it is clear that the Amended Complaint sets forth valid claims for recovery under the Act.

POINT V

The defendants' contention that "lack of registration", rather than owning and exchanging securities, was the "illegal aspect" of defendants' violations of Section 4(a).

It is only in the Layton Brief (pp. 10-13) that the defendants attempt to meet, rather than to avoid or obscure, the basic and important question of statutory interpretation involved in this case. The defendants there argue that since Section 4(a) forbade a holding company to own or exchange securities "unless registered", the "essence of the offense" is failure to register, and a valid claim for violation of Section 4(a) must therefore allege that the damages complained of resulted from "failure to register", as held by the Circuit Court of Appeals below. In addition to the answer to this argument set forth at pages 24-39 of Petitioner's Brief, the attention of the Court is respectfully directed to the following considerations.

Upon the passage of the Act the defendants had a choice between causing United to become a registered holding company or causing it to remain unregistered. If United registered, it and the defendants became subject to the provisions of the Act relating to registered holding companies and their officers, director and affiliates. If United remained unregistered, it was forbidden to own or exchange securities or to do any of the other acts prohibited by Section 4(a). Rather than submit to the consequences to their domination over United and the entire holding-company system which they feared would result from becoming a registered holding company, the defendants decided to cause United

to remain unregistered, but to continue to operate in violation of the express prohibitions of Section 4(a). It was the defendants' own choice. Having chosen to have United remain unregistered, United became subject to the prohibitions of Section 4(a) applicable to unregistered holding companies.

The defendants then argue (Layton Brief, p. 11) that Section 4(a) made it unlawful for United to sell the securities of its subsidiaries as well as for it to continue to own them. Assuming that this is so,* it is submitted that this constitutes no reason to relieve the defendants of civil liability for the damages which in fact resulted from their

---

* It is not clear that this assumption is correct. Although selling and distributing securities as an incident to the continued operation of United would undoubtedly have constituted a violation of Section 4(a)(3), it is open to question whether a distribution to its stockholders of the securities of its subsidiaries as a step in the termination of its operations would properly be construed as a violation of that section. Viewed against the background of abuses of unregulated holding companies which Congress was attempting to eliminate, it would appear that the sales of securities intended to be proscribed were only those effectuated as part of the continued operation of an unregistered holding company employing the mails and the instrumentalities of interstate commerce, and not those sales or distributions effectuated as an incident to going out of business. This conclusion is strongly reinforced by the fact that it would have been impossible for a large holding company, such as United, to continue in business if it refrained from doing all the acts proscribed by Section 4(a). In this connection it may be noted that Section 7(a) of the Investment Company Act of 1940 (54 Stat. 847, 15 U. S. C. A. §80a-7), which parallels Section 4(a) of the Public Utility Holding Company Act of 1935, expressly states that its provisions "shall not apply to transactions which are merely incidental to the dissolution of an investment company." In the light of the similar structure of the two statutes, it would appear that the foregoing provision in the Investment Company Act of 1940 merely makes explicit what was implicit in both acts even without that provision.

unlawful action in causing United to continue to own securities in violation of Section 4(a). Having embarked upon an unlawful course of action, the defendants acted at their peril. The dilemma in which they found themselves, as the result of causing United to remain unregistered, was of their own making.

Conclusion

The basic question presented by this case is the extent to which the Public Utility Holding Company Act of 1935 creates civil liability for violations of Section 4(a). The determination of this question necessarily involves a determination as to the correct construction and interpretation of that section. Under the established doctrine of *Texas & Pacific R.R. Co.* v. *Rigsby*, 241 U. S. 33, as applied to violations of Section 4(a) by the Circuit Court of Appeals for the Second Circuit in *Goldstein* v. *Groesbeck, et al.*, the first and second causes of action of the Amended Complaint set forth valid claims for damages against the defendants in this case. Under the restricted interpretation placed upon Section 4(a) by the Circuit Court of Appeals below, the first two causes of action fail to state such valid claims.

The determination of which rule of interpretation is correct, or whether some other standard of interpretation is applicable, involves an important question of interpretation of a federal statute, which is of general importance to members of the public as well as to the thousands of stockholders of The United Corporation. As alleged in the

Amended Complaint, the defendants in this case willfully violated a statute whose language was unequivocal and whose intention to prohibit the acts complained of was clear. The only question which was not clear was the extent to which the defendants might be held answerable for their actions in a civil suit. In determining the extent to which civil liability should be imposed, it is submitted that this Court should properly give application to its pronouncement in the case of *U. S.* v. *United Mine Workers*, 67 S. Ct. 677, at p. 705:

> "The greater the power that defies the law the less tolerant can this Court be of defiance."

Respectfully submitted,

JAMES R. MORFORD,
Counsel for Petitioner.

RALPH BERNSTEIN,
WILLIAM H. BENNETHUM,
JOHN F. DAVIDSON,
of Counsel.